

CONFIDENTIAL

THE DIRECTOR OF CENTRAL INTELLIGENCE

WASHINGTON, D.C. 20505

National Intelligence Council

10 June 1982

MEMORANDUM FOR: Ambassador Charles Meissner
Bureau of Economic & Business Affairs
Department of State

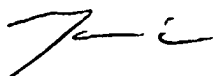
FROM: Maurice C. Ernst
National Intelligence Officer for Economics

SUBJECT: Draft Paper for NATO Meeting

Dear Chuck,

1. This is a quick draft of the paper you requested that would be tabled at the NATO East-West Economic meeting as an example of what we have in mind for presentation to the NATO Council after a new meeting in September. Section 1, Major Conclusions, is verbatim the agreed "dossier" which I prepared for the seven nations involved in the Buckley discussions, including the changes in my draft made at the request of the other nations. Section 2, Policy Implications, just raises some questions without trying to answer them. We could expand on these questions if necessary. Section 3 concerns some recommendations for the NATO Council.

2. I await your reactions and comments before giving this any further circulation for information or clearance.



Maurice C. Ernst

Attachment,
As stated

CONFIDENTIAL

THE SOVIET HARD CURRENCY POSITION AND PROSPECTS

I. Major Conclusions

The Current Situation

-- The Soviet hard currency position has worsened in the last 18 months as a result of falling oil prices, poor harvests, sluggish Western markets and Poland's financial needs.

-- In response to this situation the USSR has sold more gold in a depressed market, cut imports and increased its use of short term credit.

-- Gross Soviet debt at the end of 1981 totaled \$21 billion. With hard currency assets of about \$8 billion in Western banks, net debt amounted to about \$12.6 billion.

-- Net debt service payments amounted to about \$5 billion in 1981, which results in a moderate debt service ratio of under 20 percent.

Prospects for Soviet Hard Currency Earnings

The purchasing power of Soviet hard currency earnings is unlikely to increase and may decline during the next few years (through the mid-1980s).

o The volume of oil exports to the West will probably continue to decline; oil prices have fallen sharply in real terms during the past year and oil market conditions do not appear conducive for a price increase in real terms in the next few years.

o Higher Soviet earnings from gas exports will probably not offset the decline in oil exports at least until the Yamal pipeline is completed.

o Prospects for other Soviet exports are mixed: although exports of some products, especially chemicals, should increase, it will be difficult for the Soviets to avoid declines in earnings from exports of wood and arms.

CONFIDENTIAL

CONFIDENTIAL

Export prospects for the late 1980s and beyond are far more uncertain than those for the next few years. Oil export volume may decline further or oil exports may cease; on the other hand real oil prices may increase, and there would be time to develop other exports.

Soviet Import Possibilities

The Soviets apparently have been planning for increases of 2 to 3 percent a year in the volume of imports from the West during 1981-85.

The performance of the Soviet economy has been far worse than planned, both in industry and in agriculture. The longer-term outlook is for a rate of Soviet economic growth inadequate to sustain the rapid expansion of military spending while at the same time raising consumer welfare--in other words, the Soviet economic setting will be greatly different than in the past.

A deterioration of economic performance will make additional imports from the West especially valuable to the USSR. But if Soviet export earnings stagnate or decline in the next few years, imports cannot be increased without a growing net outflow of Western capital to the USSR, which would mean a further increase in the Soviet hard currency debt.

In past years, Moscow has followed cautious balance of payments and debt policies, but to avoid a substantial accumulation of hard currency debt will require painful steps on Moscow's part. Additional import cuts would involve either very high priority projects, major products in short supply, especially steel, or politically sensitive grain imports.

CONFIDENTIAL

II. Policy Implications

Western policies concerning trade with and credits to the Soviet Bloc can strongly influence how the Soviets deal with this problem and the manner in which their choices impinge on Western security interests. More specifically, NATO needs to consider whether, how, and to what extent Western credit policies may affect:

- o Soviet military expenditures and programs;
- o Soviet involvement in the Third World;
- o Soviet political relations with the West;
- o Soviet political and economic relations with Eastern Europe;
- o The political stability of Eastern Europe.

III. Recommendations for the NATO Council

The NATO Council and Secretariat should expand and give greater prominence to its activities on East-West economic relations, including data collection and exchange, and preparation of assessments with a view to developing a common understanding of issues and common policies on matters affecting the alliance.

Specifically, we recommend:

1. Collection on a biannual basis of data from member countries on credits to and debt due from each Eastern Bloc country and distribution of this data to all other member countries on a confidential basis. The specific reporting requirements will be developed by the Economic Directorate on the basis of consultations with a working group of experts from the capitals.

CONFIDENTIAL

2. Preparation of assessment by experts on a biannual basis on the implications of changes in trade with and credits to Eastern Bloc countries for the economy, balance of payments, and hard currency debt of these countries and their Western partners.

3. Preparation by national policy officials and experts on a biannual basis for consideration by the NATO Council of brief papers which would provide:

- a. The main conclusions of the experts' assessment, including areas of consensus and areas and reasons for disagreements;
- b. A statement of the policy implications of this assessment for the alliance;
- c. Recommendations for action by the Council.

CONFIDENTIAL